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SUBJECT: MALAYSIA UPGRADING ITS MIDDLE EAST TRADE RELATIONS

Sensitive But Unclassified

Summary and Introduction

¶11. (SBU) Recent visits of senior Malaysian government officials to the Middle East have highlighted Malaysia's interest in expanding its trade and investment ties with the region, seemingly in parallel with Malaysia's new diplomatic focus on West Asia. Malaysian trade with the region is growing strongly, and Malaysia hopes to maintain such growth by promoting sectors in which it has strong expertise, in particular the construction of large infrastructure projects.

Malaysia is reinvigorating its long-moribund joint trade committees in the region, is leading attempts to reach a trade preferential system among members of the Organization of the Islamic Conference (OIC), and recently suggested the time had come for it to consider FTA negotiations with the Gulf Cooperation Council (GCC) countries. Despite the recent strong growth and the high-level attention, however, Malaysia's trade with the region constitutes less than 4% of its total trade. The United States and countries in East and Southeast Asia will remain Malaysia's principal trade and investment partners for the foreseeable future. End Summary.

¶12. (U) Senior Malaysian government officials, including the Prime Minister, Deputy Prime Minister and several other ministers, have promoted stronger economic ties with the Middle East on recent visits to that region. Trade Minister Rafidah Aziz returned to the region in late March for a follow-up trade and investment mission to the UAE, Qatar, Bahrain and Saudi Arabia. Though these trips apparently were scheduled some time ago, and the PM is traveling frequently to the region given his position as chair of the Organization of the Islamic Conference (OIC), these visits reflect the increasing economic importance of the region to Malaysia.

Fast-Expanding Two-Way Trade

¶13. (U) According to Malaysian government statistics, two-way trade between Malaysia and West Asia (which it defines as the countries of the Arabian Peninsula, as well as Iran, Iraq, Syria, Jordan, Lebanon, and Turkey) amounted to 29.5 billion Malaysian ringgit (approximately USD 8.5 billion) in 2006, an increase of over 30 percent from 2005. Imports from West Asia to Malaysia increased by 40.4% while Malaysian exports to the region increased by 20.8% in 2006 compared to 2005. Malaysia's largest trading partner in the region is the

United Arab Emirates, accounting for 30.6% of Malaysia's trade with the region, followed by Saudi Arabia (27.1%), Iran (9.8%), Oman (9.4%), Turkey (6.7%), and Kuwait (4.4%). The region's largest single exporter to Malaysia is Saudi Arabia (with 42.3% of the region's exports), while the UAE is the largest importer from Malaysia (45.2% of Malaysian exports to West Asia).

The PM Pushes Trade and Investment Opportunities

¶4. (U) Prime Minister Abdullah Badawi's late February visit to Syria included an announcement that Syria is seeking Malaysia's participation in completing the remaining 60 kilometers of the Damascus Ring Road, a project reportedly worth 2.5 billion Malaysian ringgit (USD 714 million). Abdullah also announced other Malaysian-Syrian joint ventures worth 1.8 billion Malaysian ringgit (USD 515 million) in the areas of real estate development and higher education. Malaysian Works Minister Samy Vellu further noted that Syria was seeking Malaysian participation in the design of a new international airport and the construction of low cost houses as well as hospitals.

¶5. (U) At Abdullah's subsequent stop in Yemen, both countries announced the establishment of a joint trade committee (JTC) to facilitate bilateral trade and investment, to be chaired by the trade and industry ministers of both countries (in Malaysia the Minister of International Trade and Industry, or MITI). Malaysian firms reportedly secured 7.68 billion ringgit (USD 2.19 billion) worth of projects, primarily for road construction and the development of power plants and power transmission projects.

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Trade Minister Rafidah Keeps Up The Pressure

¶6. (U) Minister of International Trade and Industry Rafidah Aziz, who accompanied the PM to Syria and Yemen, returned to the Middle East in late March to lead a trade and investment mission to the UAE, Qatar, Bahrain, and Saudi Arabia. The last country on the mission includes a specific "construction marketing mission" with stops in Jeddah and Riyadh, reflecting Malaysia's intention to export its significant construction expertise. Malaysia is particularly eager to promote its construction sector since it is the only significant economic sector that has contracted in recent years, due to a general downshifting in the development of mega-infrastructure projects inside Malaysia.

¶7. (SBU) At Rafidah's stop in Dubai on March 22, she announced that Malaysia had raised the possible launch of free trade agreement (FTA) negotiations with the Gulf Cooperation Council (GCC) countries (Saudi Arabia, Bahrain, Kuwait, Oman, Qatar and the UAE), and was waiting for a response from the GCC. However, Ho Siew Ching, Principal Assistant Director for West Asia at MITI, told econoff that any launch of an FTA with the GCC, or with any of its member states, was not imminent, due in part to resource constraints within MITI that inhibit its ability to launch new FTA negotiations. Malaysia was more likely to continue using its JTCs, which it now has with most of the region's countries (except Saudi Arabia and Bahrain), as forums for government-to-government discussions on trade and investment.

These JTCs, similar to the Trade and Investment Framework Agreements that the United States has signed with many countries, have been in place with many of the region's countries for several decades, but for the most part have been moribund until recently, according to Ho.

¶8. (SBU) In addition to its interests in reviving the JTCs, and in eventually launching an FTA with the GCC, Ho added that Malaysia was also a strong supporter of the OIC's long-standing goal to implement a trade preferential system

(TBS-OIC) among its members. She noted that progress was being made under PM Abdullah's OIC chairmanship, with a second round of TPS-OIC negotiations having been held in November 2006 in Turkey, and a target implementation date set for January 1, 2009.

¶ 9. (SBU) Malaysia's evolving approach to its trade relations in the Middle East increasingly is focused on oil-rich states seeking to diversify their economies into areas beyond the petroleum sector, Ho told econoff. Almost half of Malaysia's exports go to the UAE, which Malaysia sees as a good match for its most competitive sectors, including not only construction but also the ICT sector and Islamic financing. In the latter area, Malaysia is also welcoming greater participation in its own Islamic banking sector by Middle Eastern firms. Banks from Qatar, Kuwait and Saudi Arabia have received licenses from the Malaysian central bank to establish a number of branches in Malaysia, despite a history of foreign firms generally facing significant constraints in operating in this sector. Malaysia also hopes to attract increasing numbers of Mideast visitors, including for medical tourism and education.

A Businessman's View

¶ 10. (SBU) A Malaysian business leader recently told Econ Counselor about his firm's first foray into the Middle East: a project to build two wharves in Saudi Arabia. He said he was surprised at how much easier it was to do business in the Middle East, in contrast to neighboring Indonesia. As a Malay, this businessman could negotiate with his Indonesian clients in his own language. But in Saudi Arabia, he found "the decisions are faster, the corruption is lower and you know the check won't bounce." He plans to reallocate some of his promotional resources from ASEAN countries to the Arab market.

Comment

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¶ 11. (SBU) Expanding trade and investment ties with the Middle East is a strategy with few disadvantages for Malaysia. Malaysia's economy largely complements the economies of the Middle East rather than competes with them. Flush with petroleum revenue and seeking sustainable development beyond the energy sector, many of the region's countries find it attractive to do business with a country that not only has real experience in advancing development (especially when "development" means large scale infrastructure projects like highways, airports, and skyscrapers), but also is a Muslim majority state. Leveraging his OIC chair, Prime Minister Abdullah has strengthened Malaysia's political ties with the region, and lobbied for a say in Middle East peace issues. In parallel, Malaysia is using these ties to push for increasing contracts for Malaysian firms. Abdullah champions an economic and development agenda within the OIC, and promotion of greater economic linkages within the Muslim world, efforts that coincide neatly with Malaysia's own overseas trade and investment goals.

¶ 12. (SBU) Trade Minister Rafidah's statement on the possible launch of an FTA with the GCC reflects the GOM's increasing awareness that Malaysia has a lot to gain from pursuing more FTAs. An FTA with the GCC or with some of its member states would be significantly less comprehensive than the FTAs that the U.S. negotiates, which would appeal to Malaysia. Such FTAs would no doubt find favor from Malaysia's would-be partners in the Mideast, including its major trading partner the UAE which, like Malaysia, has negotiated an FTA with the United States, with no agreement reached so far.

¶ 13. (SBU) Malaysia's recent high level economic interest in the Middle East, including a potential Malaysia-GCC FTA,

appears to have more to do with its desire to expand trade and investment with friendly countries that have a lot of money to spend, rather than as a reaction to the inability, so far, for it to agree on an FTA with the U.S. Moreover, with West Asia constituting less than 4% of Malaysia's total trade with the world, an FTA with all or some of the region's countries likely would have limited impact in the near to medium term, at least compared to an FTA with the U.S., Malaysia's largest trade and investment partner.

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